

MEMORANDUM

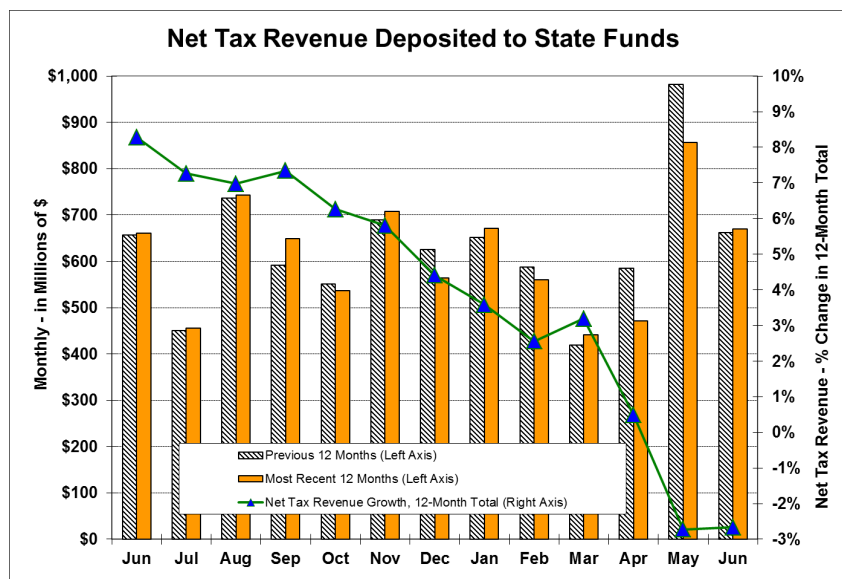
TO: Members of the Iowa Senate and
Members of the Iowa House of Representatives

FROM: Jeff Robinson
Shawn Snyder

DATE: July 18, 2014

Twelve-month Total Net Tax Receipts Through June 30, 2014

The attached spreadsheet presents net tax revenue deposited to State funds for the 12-month period ending June 2014 with comparisons to the previous 12 months. June 2013 to June 2014 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



Overview of Current Situation

The 12-month period ending June 2013 produced net State tax revenue growth of positive 9.3%. Over the 13 succeeding months, annual revenue growth turned to a decline of 2.7%. Although much of the reversal can be traced to individual income tax changes at the State and federal level, taxes paid through the purchase of fuel and cigarettes, as well as taxes paid by banks and casinos have also contributed to the downturn. With the processing of tax year 2013 individual returns complete, the income tax portion of the growth drag should now be over and future tax revenue growth will depend on economic conditions.

Month of June Comparison

June net tax receipts totaled \$670.0 million, an increase of \$8.8 million (1.3%) compared to June 2013. Major taxes and their contribution to the month's change include:

- Individual Income Tax (negative \$0.1 million, - 0.0%) – Higher income tax refunds in June resulted in flat individual income tax net receipts. Income tax withholding deposits increased 3.7% for the month.
- Sales/Use Tax (negative \$2.3 million, - 1.2%)
 - Road Use Tax Fund use tax (fee for new vehicle registration) decreased \$0.7 million.
 - General Fund sales/use tax receipts decreased \$1.6 million. Gross sales/use tax receipts increased \$1.9 million while regular tax refunds decreased \$0.5 million and school infrastructure transfers out increased \$4.0 million.
- Corporate Income Tax (positive \$15.6 million, 25.1%) – Deposits for the month increased \$9.6 million while corporate tax refunds decreased \$6.0 million.
- Fuel Tax (negative \$8.1 million, - 19.0%) – For the month of June, gross deposits decreased \$3.3 million while fuel tax refunds increased \$4.8 million. The large June decrease offsets a May increase, indicating the swing was likely the result of transaction timing.
- Cigarette and Tobacco Taxes (negative \$0.8 million, - 3.7%)
- Gambling Tax (negative \$1.2 million, - 5.1%)

Year-over-Year Comparison – Net Tax Revenue

During the 12-month period ending June 2014, net revenue from all taxes deposited to State funds totaled \$7.325 billion, a decrease of \$200.4 million (- 2.7%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$259.5 million, - 7.5%) – Annual individual income tax revenue growth peaked at \$451.4 million for the 12 months ending June 2013. Growth has declined steadily since that time. Due to an increase in the Iowa Earned Income Tax Credit, the new Taxpayer Trust Fund Tax Credit, and to the FY 2013 one-time boost to revenue that was the result of federal tax changes enacted January 1, 2013, the annual rate of income tax revenue growth declined significantly over the past several months.
- Sales/Use Tax (positive \$73.0 million, 3.0%).
- Corporate Income Tax (positive \$4.3 million, 1.0%) – Corporate income tax has been volatile in recent months and trending lower, but annual income remains modestly below its all-time high.
- Bank Tax (negative \$5.0 million, - 13.2%) – The use of income tax credits may explain the recent weakness in bank (franchise) tax receipts. Banks utilize income tax credits and often those credits are purchased from other taxpayers with insufficient tax liability to use the credits themselves.
- Fuel Tax (negative \$7.0 million, - 1.6%) – According to Department of Revenue monthly fuel sales reports, over the most recent 12-month period, Iowa taxable gasoline/ethanol gallons sold increased 1.8%. Taxable diesel sales increased 5.4%. The annual total for all taxable fuel gallons sold in Iowa is currently 1.3% below the last peak (12 months ending July 2011).
- Gambling Tax (negative \$7.9 million, - 2.7%) – According to Racing and Gaming Commission statistics, 16 of Iowa's 18 casino/track locations recorded negative annual adjusted gross revenue (AGR) growth for the 12 months ending June 2014. The combined AGR change for the 18 facilities was negative 3.9% over the previous 12 months. Across all facilities, the AGR for the most recent 12 months totaled \$1.388 billion. The annual AGR total has been declining and is 5.5% below the November 2012 peak.

- Real Estate Transfer Tax (negative \$0.3 million, - 1.6%)
- Cigarette and Tobacco Tax (negative \$4.1 million, - 1.8%)

Tax Spotlight – Sales and Use Tax

Sales of goods and services to the final user are taxed under the authority of Iowa Code [Chapter 423](#). The sale of all tangible property to the final user is subject to tax unless the tangible property is specifically exempt in Iowa Code [Section 423.3](#). The sale of services is exempt unless specifically enumerated in Iowa Code [Section 423.1\(6\)](#). With a few exceptions, items that are exempt from sales tax are also exempt from use tax.

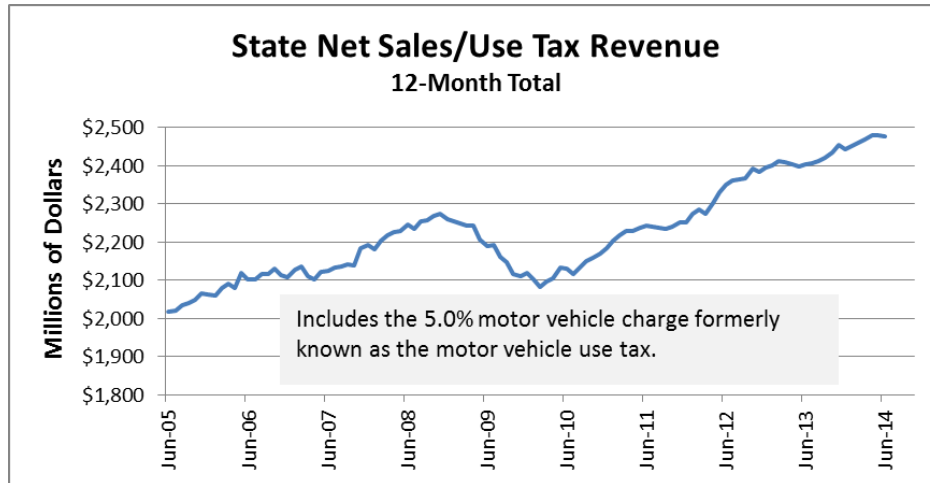
The State sales tax rate was increased to 6.0% with one-sixth of the tax devoted to school infrastructure in 2008. With the increase in the State sales tax rate, the school infrastructure local option (SILO) sales tax was repealed (this local option tax was initiated in HF 2282, Local Option Sales Tax for School Infrastructure Act of 1998). In addition to the State sales tax, with voter approval, local jurisdictions can impose a local option sales tax (LOST) of up to 1.0% (see HF 395, Local Option Sales Tax Act of 1985).

The use tax (consumer and retailer) rate was also increased to 6.0% in 2008, with one-sixth of the tax devoted to school infrastructure. The motor vehicle use tax (fee for new registration) remains at 5.0%. The use tax is not subject to LOST (except for transactions involving natural gas, natural gas services, electricity, or electric service). In general, the use tax includes:

- Tax collected by out-of-state firms making sales of tangible personal property or certain services purchased for use in Iowa (retailer's use tax).
- Tax on goods or services purchased tax free by consumers and subsequently used in Iowa (consumer's use tax).
- Tax (fee for new registration) collected by Iowa county treasurers or the Iowa Department of Transportation on the sale of vehicles subject to registration in Iowa.

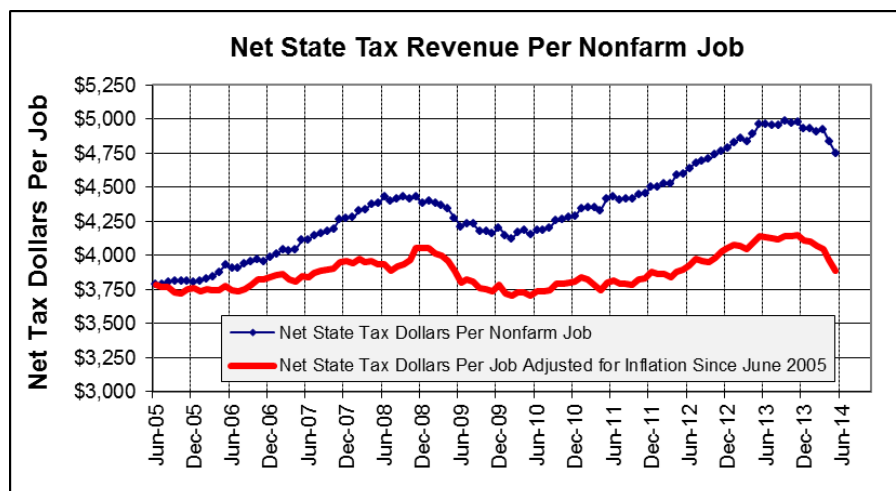
The Iowa sales tax was first imposed in 1934 in HF 1 (Net Income and Retail Sales Tax Act) for a three-year period at a rate of 2.0%. The tax was made permanent in 1937 with the passage of SF 316 (Sales Tax Act). The Iowa use tax was enacted in 1937 (SF 317 – Use Tax Act) in conjunction with the permanent adoption of the sales tax at the 2.0% rate. The tax rates were increased to 2.5% in 1955, lowered to 2.0% in 1957, increased to 3.0% in 1967, and 4.0% in 1983. The rate was changed to 5.0% in 1992. During the 2008 Legislative Session, the SILO sales tax was repealed and replaced with the 1.0 percentage point increase in the State sales/use tax in HF 2663 (State Sales/Use Tax for School Infrastructure Act of 2008).

Retailers selling tangible personal property or taxable services are responsible for collecting the State sales tax and any local option sales tax. The retailers are required to hold a retail permit and file a tax return. Depending on the amount of tax collected, deposits are due annually, quarterly, monthly, or semi-monthly. State sales tax is deposited in the State General Fund. State sales/use tax for school infrastructure and LOST are initially deposited to the State General Fund and are transferred to special funds near the end of the month. Disbursements to local entities imposing the tax are made monthly from the special funds.



Tax Revenue and Employment

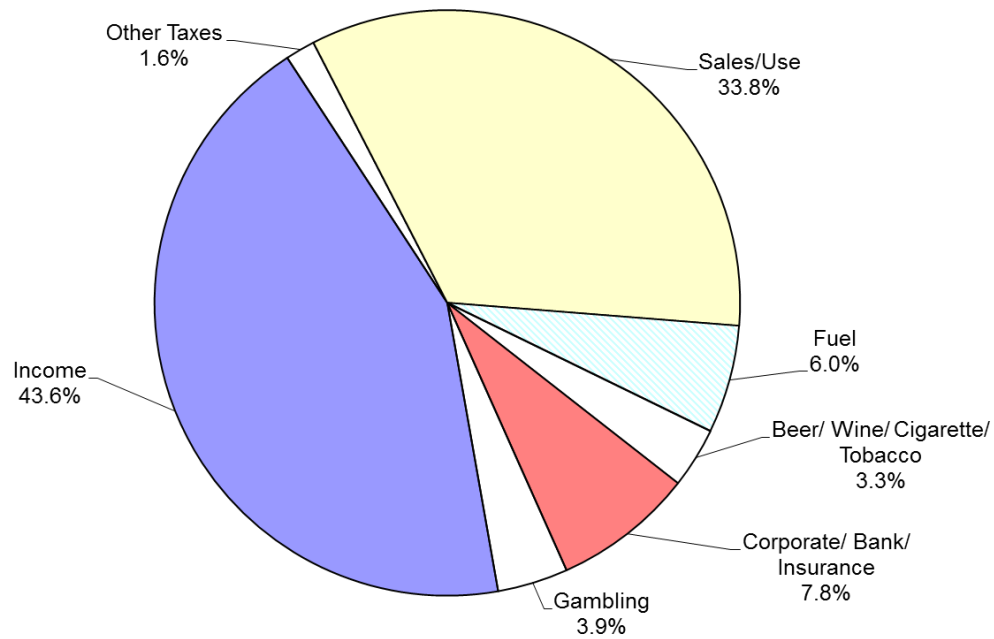
The average reading for Iowa nonfarm employment over the 12 months ending May 2014 is 1,539,800 and net State tax receipts over the same 12 months totaled \$7.316 billion, or \$4,751 per nonfarm job. This is \$966 higher than the per-job average for the 12 months ending June 2005. The blue line on the following chart depicts the annual tax revenue collected by the State per job, calculated monthly. The red line subtracts the impact of inflation since June 2005 from the blue line. The red line indicates that inflation adjusted tax revenue per job has increased \$99 since June 2005 and the remainder of the \$966 increase (\$867) represents the impact of inflation.



Net State Tax Revenue - Twelve Months Ending June 2014

Net Revenue = \$7.325 Billion

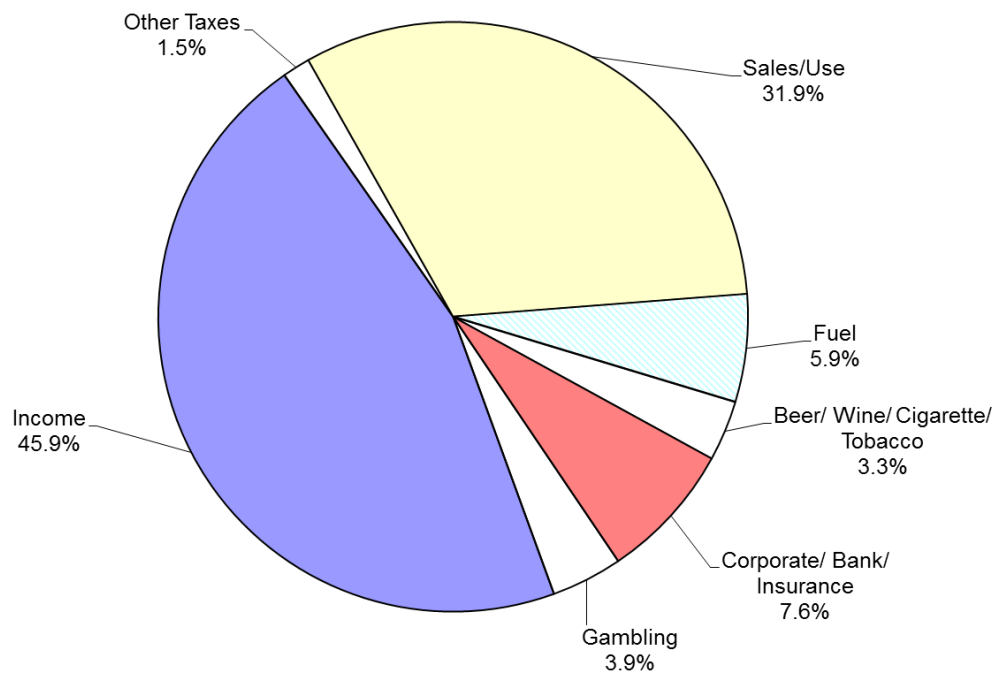
Percentages may not add to 100% due to rounding



Net State Tax Revenue - Twelve Months Ending June 2013

Net Revenue = \$7.525 Billion

Percentages may not add to 100% due to rounding



July 18, 2014

Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of June 2013	Month of June 2014	June \$ Change	June % Change
Banking	\$ 37.9	\$ 32.9	\$ - 5.0	-13.2%	\$ 5.1	\$ 7.7	\$ 2.6	51.0%
Beer & Wine	22.2	21.9	- 0.3	-1.4%	2.0	2.0	0.0	0.0%
Cigarette & Tobacco	227.0	222.9	- 4.1	-1.8%	21.7	20.9	- 0.8	-3.7%
Corporate Income	426.0	430.3	4.3	1.0%	62.2	77.8	15.6	25.1%
Fuel	443.9	436.9	- 7.0	-1.6%	42.6	34.5	- 8.1	-19.0%
Gambling	293.6	285.7	- 7.9	-2.7%	23.6	22.4	- 1.2	-5.1%
Individual Income	3,450.7	3,191.2	- 259.5	-7.5%	289.7	289.6	- 0.1	0.0%
Inheritance	85.5	89.4	3.9	4.6%	7.1	11.9	4.8	67.6%
Insurance	104.9	105.4	0.5	0.5%	17.1	15.5	- 1.6	-9.4%
Other Taxes	10.3	12.3	2.0	19.4%	0.9	0.9	0.0	0.0%
Real Estate Transfer	19.0	18.7	- 0.3	-1.6%	1.7	1.6	- 0.1	-5.9%
Sales/Use	2,404.0	2,477.0	73.0	3.0%	187.5	185.2	- 2.3	-1.2%
Total Net Taxes	\$ 7,525.0	\$ 7,324.6	\$ - 200.4	-2.7%	\$ 661.2	\$ 670.0	\$ 8.8	1.3%
Gross Tax & Refunds								
Gross Tax	\$ 8,809.4	\$ 8,796.3	\$ - 13.1	-0.1%	\$ 725.2	\$ 745.0	\$ 19.8	2.7%
Tax Refunds	\$ - 1,284.3	\$ - 1,471.7	\$ - 187.4	14.6%	\$ - 64.0	\$ - 74.8	\$ - 10.8	16.9%
Net Tax Receipts by Fund								
State General Fund (GF)	\$ 6,376.5	\$ 6,017.9	\$ - 358.6	-5.6%	\$ 563.4	\$ 561.1	\$ - 2.3	-0.4%
Road Use Tax Fund	\$ 767.4	\$ 774.7	\$ 7.3	1.0%	\$ 73.6	\$ 65.0	\$ - 8.6	-11.7%
Non-GF Gambling	\$ 250.9	\$ 284.1	\$ 33.2	13.2%	\$ 23.4	\$ 22.3	\$ - 1.1	-4.7%
Other State Funds	\$ 130.3	\$ 248.0	\$ 117.7	90.3%	\$ 0.8	\$ 21.8	\$ 21.0	2625.0%
Local Option Taxes *	\$ 874.3	\$ 908.4	\$ 34.1	3.9%	\$ 70.7	\$ 72.6	\$ 1.9	2.7%

* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

A percentage change displayed as "--" represents instances where the base year net revenue amount was zero or negative so no meaningful percentage change can be calculated.

Tax Categories Used in Table

Franchise (Bank) Tax: The franchise tax paid by banks is deposited in the State General Fund. Credit unions are taxed under a different system than banks, but the credit union tax is included in this line also. Of the total deposited, the bank tax provides approximately 98.0% of the revenue and the credit union tax 2.0%.

Beer & Liquor Tax: Taxes on beer, liquor, and wine are deposited in the State General Fund, the Liquor Control Fund, and a small amount is deposited in an Iowa Economic Development Authority fund for wine promotion.

Cigarette & Tobacco Tax: Prior to July 1, 2011, all cigarette and tobacco products tax revenue was deposited to the State General Fund. Beginning FY 2012, the first \$106.0 million of revenue from cigarette and tobacco taxes is deposited to the Health Care Trust Fund and the remainder is deposited to the State General Fund. Beginning FY 2014, all cigarette and tobacco tax revenue is deposited to the Health Care Trust Fund.

Corporate Income Tax: All corporate income tax is deposited in the State General Fund.

Motor Vehicle Fuel Tax: All motor vehicle fuel tax is deposited in one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

Gambling Tax: Gambling tax is deposited in several State funds. For FY 2013, \$40.0 million was deposited to the General Fund and the remainder to other State funds. Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, the County Endowment Fund, the Vision Iowa Fund, the Revenue Bond Debt and Subsidy Holdback Funds, the Technology Reinvestment Fund, and the Iowa Skilled Worker and Job Creation Fund.

Individual Income Tax: Most individual income tax revenue is deposited in the State General Fund. A total of \$4.0 million per year is deposited in the Workforce Development Fund. An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited in a State fund. That revenue is not included here.

Inheritance Tax: All inheritance tax is deposited in the State General Fund.

Insurance Premium Tax: All insurance premium tax is deposited in the State General Fund.

Other Taxes: Other taxes include brucellosis eradication property tax (deposited in a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

Real Estate Transfer Tax: Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The distribution of State portion of real estate transfer tax revenue is currently changing each fiscal year, with the State General Fund portion reduced to 65.0% by FY 2015. The portion not deposited to the State General Fund is deposited to the Housing Trust Fund and the Shelter Assistance Fund.

Sales/Use Tax: General sales/use tax is deposited in the State General Fund, while most vehicle use tax is deposited in the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax is referred to as a fee in the Iowa Code. To allow continuity of data, the revenue from the fee is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted from State revenue as part of the net sales/use tax calculation.

Local Option Taxes: Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Beginning FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

Report Database: The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.